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IN THE

Supreme Court of the United States

October Term, 1963
No. 624

TEMESCAL WATER COMPANY; and JAMES A. STEIN, on his own behalf and on the behalf of shareholders of Temescal Water Company,

Petitioners,

vs.

THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA,

Respondent.

Petition for a Writ of Certiorari to the Supreme Court of the State of California.

DONALD D. STARK,
Law Building,
Corona, California,
Counsel for Petitioners.

Parker & Son, Inc., Law Printers, Los Angeles. Phone MA. 6-9171.

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Respondent.

Petition for a Writ of Certiorari to the Supreme Court of the State of California.

The Petitioners pray that a writ of certiorari issue to review the judgment of the Supreme Court of the State of California affirming Decision No. 65115 of the Public Utilities Commission of the State of California.

Citation of Opinions Below.

By its Decision No. 59443 (58 Cal. P. U. C. Rep. 474) the Public Utilities Commission of the State of California, declared Temescal Water Company to be a public utility subject to the jurisdiction of the commission. The decision was affirmed by the Supreme Court of the State of California in *Corona City Water Com-*

pany v. Public Utilities Commission, (54 Cal. 2d 834, 357 P. 2d 301). By Decision No. 65115 (..... Cal. P. U. C. Rep. .....) the Commission established rates and regulations for water service, and the Supreme Court of the State of California denied a petition for a writ of certiorari or review of Decision No. 65115, without opinion. (Summary denial of the petition is an affirmance of the decision on the merits. *People v. Western Air Lines, Inc.,* 42 Cal. 2d 621, 268 P. 2d 723).

The decisions and the opinion are appended hereto as Appendix A.

Jurisdiction.

The judgment appealed from was entered on August 20, 1963. The jurisdiction of the Court is invoked under 28 U. S. C. Section 1257(3).

Questions Presented.

Is the federal requirement of due process of law offended by an order of a state regulatory agency establishing a utility rate which (a) is not based on evidence or is contrary to evidence and (b) requires in fact that the utility operate at a loss?

Is an order of a state regulatory body which applies rates and regulations for water service in derogation of existing private agreements which are not subject to public regulation a law impairing the obligation of contracts, and does such an order constitute a taking of property without due process of law?

Constitutional Provisions and Statutes Involved.

The provisions of the Constitution of the United States involved are: Article I, Section 10; Amendment XIV, Section 1.

The provision of the Constitution of the State of California involved is Article XII, Section 23.

The statutes involved are Sections 1731, 1732, 1756, and 1759 of the California Public Utilities Code.

The pertinent text of the foregoing provisions are set forth in Appendix B.

Statement of the Case.

Temescal Water Company was incorporated in 1887 for the purpose of supplying irrigation water to its shareholders only, at cost. The service area is in and around the City of Corona, Riverside County, California. Temescal operated as a private mutual water company free from public regulation until December, 1959, when the Public Utilities Commission of the State of California declared Temescal to be subject to utility regulation. The decision was upheld by the Supreme Court of the State of California (App. A: Dec. 59443; *Corona City Water Co. v. P. U. C.*).

The commission then reopened the hearing to establish rates and regulations for water service. Pending an opportunity to complete its original cost and depreciation reserve studies and the reorganization of its books to conform to the commission's regulations for public utility accounting practices, Temescal had proposed to

continue to operate under its existing nonprofit rate structure [Tem. R. 21-31].[1] On the other hand, although the commission acknowledged that there was nothing in the record to enable it to establish a rate base or to determine the water operating expenses alone, it rejected Temescal's proposal in favor of one designed by the commission's own staff "approximating" present water service revenues. The rate would provide total revenues from water sales during 1961 in an amount $40,547 short of annual expenditures [Tem. R. 31-37].

Upon receipt of Decision No. 65115 Temescal applied to the commission for a rehearing, pointing out that the rate was arbitrarily devised and confiscatory, and further showed that the rate would have resulted in a loss for 1962 of $77,440 [Tem. R. 48-52, 55-58]. The petition was nevertheless denied by the commission [Tem. R. 60-61].

Temescal thereafter petitioned the Supreme Court of the State of California for a writ of review, its only remedy under the circumstances (App. B: Secs. 1731, 1732, 1756 and 1759, Cal. P. U. Code), describing the matters set forth above and praying that the commission be commanded to certify the record to that Court for review. The petition was denied, without opinion [Tem. R. 5-12, 121].

Concerning the petition of James A. Stein, he and other owners of a total of 4,343 shares in Temescal had appeared before the commission as interested parties after the *Corona City Water Company* case, *supra*, was decided, to give evidence that they received water

[1]There are two Transcripts of Records filed herewith: Temescal v. P.U.C., SF 21396, herein "Tem. R."; Stein v. P.U.C., SF 21397, herein "St. R."

from Temescal for the irrigation of citrus crops and that the nature of this undertaking of Temescal has created private rights in the stockholders which are not subject to public regulation [St. R. 4-6].

In Decision No. 65115 the commission discarded this evidence, holding that the matter had been already decided by the *Corona City Water Company* case [St. R. 33-34]. Stein and the irrigation stockholders represented by him were likewise unsuccessful in their petition for rehearing before the commission and petition for a writ of review before the Supreme Court of the State of California, notwithstanding their claim of private right in the price and terms of the irrigation water supply and their insistence that the claim is borne out by evidence before the commission [St. R. 4-6, 40-46, 51-52, 94-101, 102].

This petition ensued.

Federal Question.

The federal questions sought to be reviewed here were raised in the petition for rehearing of Decision No. 65115 before the Public Utilities Commission of the State of California, and in the petition for a writ of review before the Supreme Court of the State of California. In ruling upon these petitions, neither the commission nor the Court made any reference to the claims of petitioners of rights under the Constitution of the United States.

The pertinent quotations of the portions of the record are set forth in Appendix C and will show that the federal question was timely and properly raised so as to give this Court jurisdiction to review the judgment on writ of certiorari.

Reasons for Granting the Writ.

The Supreme Court of the State of California has decided the federal questions involved in this petition in a way not in accord with the applicable decisions of this Court.

As to the first question sought to be reviewed here, particular reference is made to *Northern Pacific Ry. Co. v. Department of Public Works*, 45 S. Ct. 412, 268 U. S. 39, 69 L. Ed. 837, in which this Court held that an order of a state regulatory agency establishing a utility rate which is not based on evidence or is contrary to the evidence, and is confiscatory, is a denial of due process. As set forth in the statement of the case, Temescal has insisted that the rate order of the Public Utilities Commission of the State of California as embodied in Decision No. 65115 is either based upon speculation or contrary to demonstrated fact, and is confiscatory.

With reference to the second question sought to be reviewed here, the settled rule in California is that a water company may engage in part in public service and in part in private service, and the Supreme Court of the State of California has itself heretofore acknowledged that the contract of private service is protected by the prohibition of the federal constitution of state laws impairing the obligation of contract and of state action depriving a person of property without due process of law (*Allen v. Railroad Commission*, 179 Cal. 68, 175 Pac. 466).

The questions presented here are important. In Southern California the pressure of population growth and attendant competition for a water supply make it inevitable that an increasing number of nonprofit mutual water companies will face the possibility of public utility regulation. By its summary denial of the petition of Temescal and Stein for a writ of review of Decision No. 65115 of the commission, the Supreme Court of the State of California has not only denied the petitioners rights under the federal constitution but also has placed the law in a condition of uncertainty and confusion as to the rights of others similarily situated.

Respectfully submitted,

DONALD D. STARK,
Counsel for Petitioners.

APPENDIX A.

Decision No. 59443.

Before the Public Utilities Commission of the State of California.

In the matter of the application of the Corona City Water Company, a California corporation, for an order authorizing the sale and transfer of certain assets. Application No. 38626.

Investigation on the Commission's own motion into the status of Temescal Water Company and into operations, rates and practices of Temescal Water Company and Corona City Water Company. Case No. 6098.

INTERIM OPINION

By Application No. 38626, filed on November 30, 1956, Corona City Water Company, a California corporation, hereinafter referred to as Corona, seeks authority to sell two wells, only one of which is usable, and three well sites, all heretofore acquired from Coronita Mutual Water Company, to Temescal Water Company, a mutual water company, hereinafter referred to as Temescal, for the sum of $4,100. Public hearings on the application were held on May 8 and October 23, 1957, evidence was presented, and the matter was submitted. Thereafter, on May 13, 1958, the Commission made its Order Reopening for Further Hearing and Consolidation Thereof with Order Instituting Investigation. The Order Instituting Investigation referred to is the Investigation of the Commission's own motion into the status of Temescal Water Company and into the operations, rates and practices of Temescal Water Company and Corona City Water Com-

pany, Case No. 6098, filed by this Commission on May 13, 1958.

Thereafter, public hearings on the two consolidated matters were held in Los Angeles before Commissioner Theodore H. Jenner and Examiner Kent C. Rogers on April 16 and May 13, 1959, and the matters were ordered submitted thirty days after the filing of briefs. These briefs were filed on August 4, 1959. Subsequently an Examiner's Proposed Report on the matter was issued September 14, 1959. The staff filed exceptions thereto on October 5, 1959. On October 20, 1959, the applicant and respondents filed their reply to said exceptions.

By Application No. 38626, Corona seeks authority to transfer the heretofore described property to Temescal for the sum of $4,100. By Decision No. 52396, dated December 22, 1955, in Application No. 37390, the Commission had required that Corona retain said property "until and unless the Commission shall otherwise order".

History of Corona and Temescal

Temescal was organized under the laws of the State of California on March 22, 1887, for the purpose of furnishing and distributing water to its shareholders at cost. It obtains its water from wells, canyon streams, and Metropolitan Water District, and through ownership of stock in other water companies.

As of December 31, 1957, Temescal had 11,759 shares of stock outstanding, of which 2,100 were held by Corona.

Temescal has supplied its stockholders with water for approximately 70 years, gradually acquiring land,

water rights, reservoirs, wells, pumping plants, canals, pipelines, and stock in other water companies.

The history of the Temescal system dates back to 1880 when the South Riverside Land and Water Company began the development of a large area for citrus culture which included the present city limits of Corona City. Early subdivision of the land was known as the townsite of South Riverside, since renamed Corona. The water supply required for this development was obtained from the Temescal River Basin and a water system was constructed to furnish the territory with irrigation and domestic water.

Temescal was formed in 1887 to acquire the water system referred to above, including all sources of supply and territory, to separate the land transactions of the South Riverside Land and Water Company from the water supply operations.

The Iowa-California Land Company was formed in the meantime, and acquired the right to subdivide the town lots and the right to install and operate a distribution pipe system in the town for domestic purposes. The water supply for this domestic utility was obtained from Temescal through the purchase of 500 shares of Temescal stock.

In 1897 Temescal organized Corona which acquired the property, rights and all interests of the Iowa-California Land Company in the domestic water system. To meet the growth and development of the City of Corona and the increased demand for water, the utility made additions, extensions and improvements to the distribution system, but in lieu of developing its own water supply, it obtained additional water from Temescal.

In addition to the water supply from the Temescal River Basin, Temescal later developed wells in the City of Corona and connected these directly to Corona's distribution system. At the present time Temescal has four wells in the city (not including the Coronita well referred to in Application No. 38626).

All of the common stock of Corona, 750 shares, is held for the stockholders of Temescal under a trust agreement dated December 6, 1923. As of July 31, 1958, the trustees were: Joy G. Jameson, Jr., R. L. Hampton and Lucile Burns. Mr. C. M. Brewer is the general manager of each company.

The directors of each company consisted of the following on July 31, 1958:

R. L. Hampton	R. C. Verity
A. C. Barns	T. J. Todd
E. F. Birdsall	Joy G. Jameson, Jr.
R. L. Cook	

As of July 31, 1958, the respective officers were as follows:

Officers	Corona	Temescal
R. L. Hampton	.....	President
Joy G. Jameson, Jr.	President	Vice-President
R. C. Verity	Vice-President	.....
Lucile Burns	Sec.-Treasurer	Sec.-Treasurer
C. M. Brewer	Asst. Sec.-Treas.	Asst. Sec.-Treas.

Temescal Stock Held by Corona

Disregarding the Coronita well, all of Corona's water is secured from Temescal through stock issued by Temescal to Corona. As of April 15, 1959, Corona had 2100 shares of Temescal stock issued between 1897 and 1956 which was purchased by Corona for prices ranging from $125 to $185 and at a total cost to Corona of $316,500.

There are two types of stock issued by Temescal. The first is canyon line stock which sells for $50 per share and entitles the holder thereof only to water from the Metropolitan Water District. Common stock is of one class only. The stock is not appurtenant to the land but limits the water entitlement and may be affixed to any location in Temescal's service area. The presently authorized price of stock is $185 per share. Temescal has various lines bringing water into the service area (see Exhibit No. 11), including the high line and the low line. The high line is to the south at a higher elevation (Line No. 3). Historically, due to higher pumping costs, a $60 per share premium was charged for changing low line to high line shares. All stock recently acquired by Corona is high line shares. At present no high line or low line stock is available. It becomes available as subdivisions are formed and agricultural areas changed to residential.

Disregarding the canyon line shares, all Temescal stock is entitled to the same amount of water, basically, one-tenth of a miner's inch of water per day per share, but the amount is varied by Temescal's directors. To obtain expense money, the directors determine and collect an annual assessment for each share of stock. The assessment was $18 per share in 1956 and 1957, and $21 per share in 1958. Except for Corona, the majority of Temescal customers are agricultural, and water allowances per share are based on irrigation requirements. However, Temescal furnishes water to a number of commercial and domestic customers. When no irrigation is needed, no water allowances are made. This means that when adequate water is available due to the fact that no agricultural users require water,

Corona must buy so-called "extra water" at $1.10 per miner's inch day as the directors of Temescal make no water allowance per share of stock. Each agricultural user must use his water entitlement in the month in which it is granted by Temescal (except for a 5% carry over into the next month), but Corona is permitted to compute its water usage on an annual basis and pay only for extra water above the entire year's cumulative stock allowance.

The System

Temescal secures its water from various sources in the vicinity of Lake Elsinore and by importing water from the San Bernardino basin which it obtains by means of stock ownership in various other water companies. It also has wells in the vicinity of Glen Ivy southeast of Corona, and wells in the City of Corona. Lines run from the various sources into the vicinity of Corona. As most of the consumers of Temescal are irrigation or commercial, none of the water is treated except that which is used by Temescal to supply the City of Corona and other domestic consumers. Line No. 3, the so-called high line, extends from Glen Ivy into Corona. The water carried in the line is treated and there are numerous water consumers outside the City of Corona and outside the service area of Corona City Water Company who receive water direct from this line. Outside the City of Corona the line is owned by Temescal, and inside the city it is owned by Corona (see Exhibits Nos. 10 and 11). Said line is operated by Temescal.

Domestic and Commercial Water Consumers (nonstockholders of Temescal) Securing Water From the Temescal Transmission Lines and Stockholders of Temescal Securing Water From the Corona Lines

There are several water consumers, both domestic and commercial, outside Corona's certificated area along the No. 3 or high line between Glen Ivy and the Corona City Limits who are served by said line. There are also certain consumers on the irrigation line who receive non-potable water for fire protection and commercial uses. None of these consumers are stockholders of Temescal. Temescal argues that these consumers are customers of Corona as Corona meters the service, bills and collects for the water. [1] However, it is clear these consumers are located outside any area which Corona has a certificate to serve; they are served directly from Temescal's lines, the only facilities of Corona involved being a meter at the premises, and in the case of the commercial users, receive nonpotable water and in some instances "interruptible service" for which Corona has no filed tariff and therefore is not authorized to provide. The funds collected by Corona for these services eventually find their way to Temescal or Temescal's stockholders either by way of water purchases by Corona for these consumers or through the trust declaration heretofore referred to. This arrangement and practice between Temescal and Corona, we find to be a scheme and device employed by these parties to shield Temescal from regulation by this Commission and a device to violate the applicable regulatory statute.

In its service area Corona supplies water to several of Temescal stockholders. Corona does not bill these

consumers and the water received by them is considered by both Temescal and Corona as water supplied under stock entitlement. At about the time this investigation was instituted, Corona and Temescal began offsetting the amount of water these consumers received against the water charged to Corona by Temescal. Again, Corona has no provision in its tariff for this type of service and Corona is not compensated by Temescal for the use of its facilities in serving these consumers.

It is apparent that the operations of Temescal and Corona, considered as a whole, form an integrated system and that Corona is dominated and controlled in its entirety by Temescal whose interests lie mainly with its agricultural stockholders.

It is equally apparent that it would be an illegal extension of its service for Corona to acquire customers outside its service area or to furnish services not provided for in its tariffs without prior authority from this Commission. All of the foregoing of this Interim Opinion we hereby find to be the fact based upon the record herein.

In light of the record in this case, this Commission cannot recognize the hereinabove-described water consumers as customers of Corona, for to do so would be to accept an illegal activity of Temescal's subordinate affiliate, Corona, as lawful.

This Commission finds that these consumers are in fact customers of Temescal and that the activities of Corona in connection therewith constitute the activities of an agent in behalf of its principal.

Among the issues raised herein are whether or not Temescal is a mutual water company, whether or not

Temescal is a public utility water company, and whether or not Corona is the alter ego of Temescal and vice versa.

Temescal was formed as a mutual water company. The Articles of Incorporation of the company (Exhibit No. 6) provide that

> "the primary purpose for which this company is formed is to acquire, own and hold water and water rights, to construct and maintain waterworks and storage and distribution facilities, for the purpose of furnishing and distributing water to its shareholders only, at cost."

However, it is clear that even though organized as a mutual, a water company can become a utility by its subsequent activities. *Western Canal vs. Railroad Commission*, 216 Cal. 639, 646-647.

The evidence herein shows, and we find, that Temescal delivers water to persons other than its stockholders or members contrary to the provisions of Section 2705 of the Public Utilities Code and, therefore, Temescal's operations fall squarely within the provisions of Sections 2702 and 2703 of that Code, which latter sections are the counterpart of Section 2705. This finding is sufficient to subject Temescal to the jurisdiction of this Commission.

Furthermore, Temescal has presented no evidence that its water deliveries are "at cost," which is another requirement of Section 2705. It has neglected to make a cost of service study to apportion costs in serving its stockholders and has refused the staff of the Commission access to its books for the purpose of making such a study. We can only conclude, therefore, that this

evidence, if presented, would be adverse to Temescal (C.C.P., Sec. 1963, sub. 5). Temescal presented figures purporting to show that, for some period of time, it operated at a loss. This does not prove that it delivers water at cost. Many public utilities fail to earn their expenses for long periods of time. Finally, as Public Utilities Code Section 2705 is an exemption statute, it provides an affirmative defense to regulation as a public utility and the burden is upon Temescal to prove that each and every requirement in said section is fully satisfied before the exemption will apply (C.C.P., Sections 1869, 1981). The evidence of record shows and we find that Temescal has failed to prove that its deliveries of water are at cost and that it delivers water to those named in Section 2705. It is elementary that the burden rests upon the party claiming exemption from regulation, where but for the exemption such party would be subject thereto, to prove his entitlement to such exemption. (*Piedmont & Northern Ry. Co. vs. I.C.C.*, 286 U. S. 299, 311, 312, 76 L. ed. 1115, 1123; *Interstate Natural Gas Co. vs. F.P.C.*, 331 U.S. 682, 691, 91 L. ed. 1742, 1748; *U.S. vs. Public Utilities Commission of California*, 345 U. S. 295, 310, 97 L. ed. 1020, 1034.) See also our recent decision in Yucaipa Domestic Water Co. vs. Yucaipa Water Co. No. 1, Decision No. 59222, Cases Nos. 6247-6248. Thus, we find that Temescal is not exempted from regulation as a public utility by the provisions of Public Utilities Code Section 2705.

Additionally, the evidence shows and we find that Temescal supplies water to Corona (in fact is the sole supplier) which brings Temescal squarely within the provisions of Section 216(c) of the Public Utilities Code which defines a public utility as a person or corpora-

tion performing any service or delivering any commodity to any person, private corporation, municipality or other political subdivision of the State, which, in turn, either directly or indirectly, mediately or immediately, performs such service or delivers such commodity to or for the public or some portion thereof. The water delivered by Temescal to Corona is redelivered by Corona to its customers and we hereby so find. The language of Section 216(c) is clear and unambiguous and was added to the Public Utilities Act in 1913 to overcome contentions then being made which sought to avoid regulation.

The issue of alter ego is presented and the staff of the Commission points out that there is an identity of directors and partial identity of officers of Temescal and Corona. Moreover, the same person is general manager of both companies. They share the same offices and as previously pointed out some facilities of each are used interchangeably by both for their mutual convenience. Corona is a stockholder of Temescal and all of Corona's outstanding stock is held by a board of trustees for the benefit of Temescal's shareholders.

The staff further points out that an adherence to the fiction of a separate existence of Temescal and Corona would promote an injustice in that it would sanction and recognize a legal fiction obviously created by Temescal expressly to evade and frustrate regulation of its operations by this Commission. It is elementary that this Commission, in the exercise of its constitutional and statutory duties, cannot permit Temescal to accomplish by means of a scheme or device or legal fiction, that which it cannot accomplish directly, *i.e.*, engage in business of a public utility water company

free from regulation by this Commission. On this issue we find the facts to be as follows.

It is undisputed that the domination and control of Corona by Temescal has prevented Corona from developing its own sources of water. Corona is utterly dependent upon Temescal for its water. Corona has been prevented from owning or operating wells which are connected directly to its distribution facilities. At the time of submission, Corona had over $300,000.00 on its books representing stock purchases in Temescal. This would normally represent an investment in capital assets for water producing facilities. However, under the present situation, this Commission has no way of determining whether this sum represents capital assets at all; or whether the money has been spent by Temescal to meet operating expenses. As the agricultural consumption of Temescal's water decreases and the domestic consumption increases in the future it can easily be foreseen that ultimately Corona will acquire by purchase a majority of Temescal's transmission facilities and water stock. Corona will still have no water production facilities and Temescal's assets will be mainly water production facilities. A presently existing example of the effect of this ultimate result is the Coronita well. If Temescal should acquire this well for $4,100.00 (as requested by Corona), Corona would then be required to pay $138,000.00 for stock in Temescal to obtain an equivalent amount of water which could be produced by the well. In addition, the annual cost to Corona in assessments and extra water charges would be approximately four times the cost of operating the well (Exhibit No. 9, Ch. 6). Under the circumstances, the injustice is apparent.

For many years, Temescal has dominated and controlled Corona. As against Temescal, Corona has no will of its own. The directors are the same and for all intents and purposes the officers are the same with immaterial exceptions. There is a unity of operation and control and, in fact and in law, the operations of these two companies constitute one integrated activity. Any separation of operations is artificial and colorable and is employed in an attempt to evade regulation. Corona is the alter ego of Temescal and vice versa. To recognize the separate existences of these two companies would defeat and frustrate lawful regulation of the activities of both these companies. The failure to regulate Temescal results in a substantial frustration of lawful regulation of Corona. The case of *Minific v. Rowley*, 187 Cal. 481, cited and relied upon by Temescal, declares no rule contrary to the principle which we follow herein. The rule applicable to alter ego has been expanded by the Supreme Court of this State since *Minific v. Rowley* was decided. However, it must be kept in mind that these court decisions dealt with adversary proceedings between private parties and not regulatory proceedings. Any scheme or device calculated to unlawfully evade or frustrate regulation constitutes constructive fraud upon the public. This subject has recently received the consideration of the Commission in a proceeding where all elements of the subject were explored fully. There the Commission found that the proof of actual fraud is not necessary to invoke the rule of alter ego. All that need be shown is that the device will defeat or frustrate regulation. In such circumstances corporate fiction will be disregarded and regulation will be administered. (*Direct Delivery Case*, 54 Cal. P.U.C. 258, 263.)

Temescal has, on two separate occasions, resorted to proceedings in eminent domain to acquire operating property (Exhibit No. 12). As the right of eminent domain may only be exercised to convert a private use to a public use (see *Northern Light & Power Co. vs. Stacher*, 13 C.A. 404 (1910), *General Petroleum Corp. vs. Hobson*, 23 F. 2d 349 (1928) and *Eckel vs. Springfield*, 87 C.A. 617 (1928)), Temescal has by the exercise of that right, made an unequivocal act of dedication to public use and is estopped to deny that it is a public utility. *Producers Transp. Co. vs. Railroad Commission*, 176 Cal. 499 (1917.).

Temescal argues, however, in its written brief, at pages 33 and 34, that "The statutes of California give the right of eminent domain to development of water for irrigation purposes (Code Civ. Proc., Sec. 1238.5), and in fact the law expressly gives this power to mutual water companies. (Code Civ. Proc., Sec. 1238, par. 4.) The granting of the power of eminent domain to mutuals and at the same time the exemption of mutuals pursuant to Section 2705 can only mean that the Legislature contemplated that the exercise of eminent domain by a mutual does not of itself result in Commission jurisdiction."

The quoted paragraph misconstrues the effect of C.C.P. 1238, et seq., and in fact ignores the first sentence of said section which states ". . . the right of eminent domain may be exercised *in behalf of the following public uses.*" Temescal also ignores C.C.P. 1237 which defines eminent domain as "the right of the people or government to take private property *for public use.*" It also ignores Civil Code Section 1001 which states "*any person may* . . . acquire private

property for *any use* specified in section twelve hundred and thirty-eight of the Code of Civil Procedure either by consent of the owner or by proceedings had under the provisions of title seven, part three, of the Code of Civil Procedure. . . ." Temescal also ignores the vital distinction between the mere existence of an incorporeal right or power and the voluntary exercise of that right. The fact that Temescal may exercise the right of eminent domain does not exempt the exercise of the right from constituting a dedication to the public use. Temescal was not compelled to exercise the right of eminent domain but it did so and such exercise converted it into a public utility, if it was not already of that status.

We need not tarry long on the issue involving the request by Corona to transfer these water wells to Temescal. We find from the evidence that these wells are necessary and useful to Corona, within the purview of the provisions of Section 851 of the Public Utilities Code, and that a transfer to Temescal would be contrary to the public interest. We find that Corona needs additional water supplies and will continue in the future to need additional water supplies. The claim made by the utility that there is a legal inhibition against it operating these wells is beside the point. This Commission cannot take this assertion by the utility as an adjudicated fact; otherwise, we would be abdicating our jurisdiction and authority to the utility. The evidence shows that the objection upon which this assertion is based was made by a party who is connected with this utility and Temescal. It appears to be a "family" matter. At all events, this asserted legal inhibition would have to be litigated in a tribunal of competent jurisdiction and if the asserted inhibition should be up-

held, this Commission has the authority to order the utility to condemn any right upon which such inhibition may be based. This asserted legal inhibition is immaterial to the issues in this proceeding. The request of Corona to transfer this property will be denied.

Conclusion

Based upon the foregoing findings of fact, the Commission concludes that Temescal is a public utility water corporation pursuant to the provisions of Sections 216, 241, 2701, 2702 and 2703 of the Public Utilities Code and that it has dedicated its properties to the public use.

In taking the action herein, the Commission is not unmindful that parties, without meaning to do so, may become subject to regulation because of the acts which they commit. This, sometimes, works a hardship upon the party thus finding himself confronted with regulatory requirements. It may well be that Temescal's owners were of the opinion that they were avoiding regulatory status but such would not be a defense against regulation, if the acts actually committed brought that company, as we have so held, within the ambit of the regulatory statute. The Commission must proceed upon the law and the facts, irrespective of the intent of the parties involved. It is not what a person intends that counts but, rather what he actually does In regulating this water operation, the Commission will administer the law in light of the historical pattern and growth of the operation, consistent with the public interest.

INTERIM ORDER

Investigation of the Commission's own motion having been instituted, and the same having been consolidated for hearing with Application No. 38626, public hearings

having been held thereon, and the matters having been submitted and now being ready for decision,

IT IS HEREBY ORDERED:

1. That Application No. 38626 is denied.

2. That Temescal Water Company is declared to be a public utility subject to the jurisdiction, supervision and control of this Commission.

3. That submission in Case No. 6098 be set aside and said case be reopened for further hearing for the purpose of determining various matters pertinent to the regulation of this utility, including, but not limited to the following:

a. Determination of the original cost, estimated if not known, of the water system properties used and useful in the public service, together with the depreciation reserve requirement applicable thereto.

b. The establishment of fair and reasonable rates and rules for this system.

The effective date of this order shall be twenty days after the date hereof.

Dated at San Francisco, California, this 29th day of December, 1959.

McKeage, *President*
Mitchell, Dooley, Fox, *Commissioners*

I concur in this interim opinion and order, except that I withhold my approval from that portion thereof in which the Commission expresses its opinion on the effect of Section 216 c of the Public Utilities Code in determining public utility status.

Jenner, *Commissioner*

Opinion of the Supreme Court of California.

[S. F. No. 20433. In Bank: Nov. 25, 1960.]

Corona City Water Company (a Corporation) et al., Petitioners, v. Public Utilities Commission of the State of California, Respondent.

Proceeding to review an order of the Public Utilities Commission denying one water company's application for permission to sell property to another water company, and determining that second water company was a public utility subject to jurisdiction of commission. Order affirmed.

Clayson, Stark & Rothrock and George G. Grover for Petitioners.

William M. Bennett, Chief Counsel, Roderick B. Cassidy, Assistant Chief Counsel, and Mary Moran Pajalich, Senior Counsel, for Respondent.

Traynor, *J.*—In this proceeding Corona City Water Company and Temescal Water Company attack an order of the Public Utilities Commission denying Corona's application for permission to sell property to Temescal and determining that Temescal is a public utility subject to the jurisdiction of the commission.

Temescal is organized as a nonpublic utility mutual water company and has not heretofore been regulated by the commission. Corona is a regulated public utility water company that secures its water from Temescal as a shareholder of Temescal stock. In 1955 Corona secured the commission's approval to buy all of the assets of the Coronita Mutual Water Company and to extend its service to the former consumers supplied by that company, on condition that it retain the water production facilities of Coronita until further order of the commission. In 1956 Corona applied to the commission for permission to sell those facilities to Temescal on

the ground that they were not useful to Corona's utility operations. Following a hearing on the application, the commission instituted an investigation on its own motion into the relationship between Corona and Temescal and the status of Temescal and reopened the hearing of Corona's application. After further hearings it found that Temescal is a public utility that has dedicated its property to public use (see Pub. Util. Code, §§ 216, 240, 241, 2701, 2702) and that it is not exempt from regulation under section 2705 of the Public Utilities Code. It also found that the water production facilities Corona obtained from Coronita were necessary and useful to Corona and denied its application for permission to sell those facilities to Temescal. Both companies join in attacking these findings.

Temescal and Corona are closely related. They have the same directors, the same secretary-treasurer, and the same general manager and assistant secretary-treasurer. One of the directors is president of Temescal, another is president of Corona and vice-president of Temescal, and a third is vice-president of Corona. Corona was organized by Temescal and owns 2,100 shares or approximately 19 percent of Temescal's outstanding stock. Before 1923 Temescal owned all of Corona's stock except for directors' qualifying shares. In that year, fearful that such ownership might affect its status as a mutual, Temescal conveyed its Corona stock to trustee to hold for the benefit of Temescal stockholders. Under the terms of the trust no beneficial interest in Corona stock can be severed from the ownership of Temescal stock, and in the administration of the trust, the "trustees shall at all times be amenable to the will and direction of the stockholders representing a majority of the subscribed capital stock" of Temescal. The trustees

are the president and secretary of Temescal and the president of Corona.

The general manager of the two companies testified that it is their policy to operate in such a way as to promote the development of the Corona area for the public benefit. Temescal has undertaken to secure the necessary water sources and production facilities to provide water for both companies, and on two occasions it has exercised the power of eminent domain to that end. In addition to supplying its other stockholders, Temescal has declared its policy to supply Corona "with water stock and water at all times to meet the full requirements of said utility and its customers." It also has authorized but unissued shares that may be purchased by persons in its service area who wish to secure water by becoming stockholders.

The physical operations of the two companies are closely integrated, and together they provide overall water service for the city of Corona and surrounding territory. Temescal has engaged primarily in securing water for itself and Corona and in delivering water to its agricultural stockholders for irrigation purposes. Corona has engaged primarily in delivering water to the public in the city of Corona for domestic purposes. As the companies have grown, however, there has been some overlapping of their functions and service areas. Thus, where it has been physically convenient to do so, Temescal has supplied water from its lines through Corona meters to nonstockholders of Temescal, and Corona has supplied water from its lines without charge to Temescal stockholders for spraying their citrus groves. Corona charges the nonstockholders for the water metered by it, but both companies consider the water delivered by Corona to Temescal stockholders as

supplied under their stock entitlement. At about the time the commission instituted its investigation, Corona and Temescal began offsetting the amount of water Temescal stockholders received from Corona against the water charged to Corona by Temescal. Corona does not charge Temescal for the use of its lines in delivering water to Temescal stockholders, however, and Temescal does not charge Corona for the use of its lines in delivering water to Corona meters.

In view of Temescal's extensive activities in close collaboration with an admitted public utility water corporation, we find no merit in Temescal's contention that it has not dedicated its property to public use. Thus, it has offered and provided unlimited service to Corona (see *Richfield Oil Corp. v. Public Util. Com.*, *ante*, pp. 419, 430, 431, 438, 439 [6 Cal. Rptr. 548, 354 P. 2d 4]), it has condemned property for public use (see *Producers Transp. Co. v. Railroad Com.*, 176 Cal. 499, 505 [169 P. 59]), and it directly serves anyone in its service area who becomes a stockholder. (See *Yucaipa Water Company No. 1 v. Public Utilities Com.*, *ante*, pp. ....., ... [9 Cal.Rptr. 239, 357 P.2d 295].)

Temescal contends, however, that even if it has dedicated its property to public use, it is exempted from public utility regulation by section 2705 of the Public Utilities Code. That section provides:

"Any corporation or association which is organized for the purpose solely of delivering water to its stockholders or members at cost, and which delivers water to no one except its stockholders or members, or to the State or any agency or department thereof, or to any school district, or to any other mutual water company, at cost, is not a public utility, and is not subject to the jurisdiction, control or regulation of the commission."

The commission contends that Temescal is not exempt from regulation under this section on the ground that it is delivering water to nonstockholders through the agency of its *alter ego* Corona, which it created and controls for the purpose of evading lawful regulation. Temescal contends that the separate corporate entities may not be disregarded unless an inequitable result would otherwise occur (see *Automotriz etc. De California v. Resnick*, 47 Cal.2d 792, 796 [306 P.2d 1, 63 A.L.R.2d 1042]) and that no such result has been shown in this case. In its view, the commission seeks to disregard the separate corporate entities, not to prevent an unlawful evasion of its jurisdiction, but solely to exert jurisdiction that the Legislature has denied it.

In *Yucaipa Water Company No. 1 v. Public Utilities Com.*, *ante*, pp. 823, 830 [9 Cal.Rptr. 239, 357 P.2d 295], we pointed out that "The exemption created by section 2705 indicates a legislative determination that when a mutual water corporation is substantially customer-controlled and delivers water at cost, the usual judicial contract remedies available to those who deal with it are an adequate substitute for public utility regulation." The reasons underlying the exemption are obviously not present, however, when, as in this case, a major customer has no voice in the management and, as the creature of the mutual and its other stockholders, is in no position effectively to enforce its rights as a stockholder. To hold that such a captive stockholder is a stockholder within the meaning of section 2705 would violate the principles on which the statute is based. Accordingly, the word "stockholder" in that section must be interpreted to mean, not a mere conduit of voting power by which the independent stockholders echo their own votes, but a bona fide stockholder that

is free independently to exercise its voice in management and to enforce its legal rights.

It is no answer to these considerations to assert that no infringement of Corona's rights has been proved in this case, for it is clear that whether or not such an infringement has occurred, the intercorporate relationship is fraught with hazards to Corona and its customers. Thus, the largely agricultural independent stockholders of Temescal are in a position to subsidize their water service at the expense of Corona and to prevent Corona's objecting by their control of it. It is the existence of such power, not just its improper exercise, that violates the principles underlying the exemption of section 2705.

The potentiality of abuse is illustrated by the position of Corona and Temescal with respect to the proposed sale of Temescal of the water production facilities Corona purchased from Coronita. Those facilities include a well from which Corona can pump water at a much lower cost than it can buy water from Temescal. Both Corona and Temescal contend, however, that Corona cannot lawfully pump water from the well on the ground that a public utility does not succeed to an overlying water right being exercised by a mutual for the benefit of its stockholders when it purchases the mutual's assets and extends service to the mutual's former stockhholders. They assert that it is only Temescal, as another mutual exercising the overlying rights of its stockholders, that can lawfully pump the Coronita well. Corona therefore proposes to sell the well to Temescal at a price that does not include the value of the water right. The commission was not convinced that Corona could not lawfully pump the well, and it pointed out that the only objection to Corona's doing so came from a citrus growing corporation that is a stock-

holder of Temescal and whose president was then president of Corona. The commission, however, refused to determine whether Corona could lawfully pump the well on the ground that the issue should be determined in appropriate litigation. We too deem it inappropriate to determine that issue in the absence of an adversary presentation of it and the presence of other interested parties. There is, however, at least an apparent anomaly in Corona's and Temescal's position that Corona cannot lawfully pump water from the Coronita well to serve Coronita's former stockholders but that Corona can supply those same consumers with the same water if Temescal pumps it for it. Were Corona not controlled by Temescal, the apparent anomaly of the position it now asserts might have indicated the wisdom of asserting and litigating a right to pump the well instead of conceding that that right did not exist.

The foregoing considerations are determinative of Corona's and Temescal's attack on the commission's refusal to permit Corona to make the proposed sale. The Coronita well is obviously valuable to Corona if Corona can lawfully pump it, and although Corona secured independent legal advice that it could not, in view of Corona's domination by Temescal and Temescal's interest in the question, the commission was justified in requiring that the issue be litigated before approving the sale. (See Pub. Util. Code, § 851.)

The order is affirmed.

Gibson, *C. J.*, Peters, *J.*, White, *J.*, and Dooling, *J.*, concurred.

McComb, *J.*, dissented.

Petitioners' application for a rehearing was denied December 21, 1960. McComb, *J.*, was of the opinion that the petition should be granted.

Decision No. 65115.

Before the Public Utilities Commission of the State of California.

Investigation on the Commission's own motion into the status of Temescal Water Company and into the operations, rates and practices of Temescal Water Company and Corona City Water Company. Case No. 6098.

Clayson, Stark, Rothrock and Mann, by *Donald D. Stark*, for Temescal Water Company.

Walker and Sullivan, by *Alexander B. Yakutis*, for shareholders of Temescal Water Company.

Elinore Charles, for the Commission staff.

OPINION

The history of this litigation commenced on November 30, 1956, when Corona City Water Company (Corona) filed its application for authority to sell two wells and some well-sites to Temescal Water Company (Temescal), then purporting to act as a mutual water company. Hearings were held on this application and the matter was submitted. Thereafter, on May 13, 1958, the Commission reopened the application for further hearing and consolidated the application with Case No. 6098, an investigation on the Commission's own motion into the status of Temescal Water Company. Hearings were held on the above matters and order by Decision No. 59443, dated December 29, 1959, in which it denied the requested authority, declared that Temescal is a public utility subject to the jurisdiction, supervision, and control of this Commission, and ordered that the submission of Case No. 6098 be set aside and the case reopened for further hearing for the purpose of determining various matters pertinent to the regulation of Temescal, including but not limited to the following:

(a) The original cost, estimated if not known, of the water system properties used and useful in the public service, together with the depreciation reserve requirement applicable thereto; and

(2) The establishment of fair and reasonable rates and rules for this system.

A petition for rehearing before the Commission was denied on February 29, 1960. On November 25, 1960, the California Supreme Court affirmed the decision of the Commission and on December 21, 1960, a rehearing was denied by the Supreme Court. Further hearings were held in Corona, California, before Examiner Rogers on May 9, 10, and 11, 1962. Oral argument was held before Commissioner Mitchell in San Francisco on July 23, 1962, at the conclusion of which the matter was submitted subject to the receipt of concurrent briefs on or before September 14, 1962. These briefs were filed and considered and the matter is ready for decision.

For the purpose of this decision, no reference will be made to the application of Corona City Water Company.

Decision No. 59443, supra, outlined the history of the litigation and the company. No additional statements thereof are necessary herein.

The Service Area

Temescal has a claimed service area mostly situated in the City of Corona, with some portions extending southeast of the city towards Lake Elsinore. It is difficult to define an existing service area inasmuch as Temescal apparently serves any entity owning land in the vicinity of Corona and Temescal Canyon and ac-

quiring sufficient stock for such service, but judging by the maps and stock issued, it appears that Temescal provides water to over 4,000 acres of agricultural land.

Stock and Stock Attributes

The Articles of Incorporation specify two types of stock, namely, common stock and Canyon Line stock. The common stock entitles the holder thereof to have irrigation water delivered in and around the City of Corona and along the transmission line from Railroad Canyon to Corona. Canyon Line stock entitles the holder thereof to water from the Metropolitan Water District only. Neither type of stock is, nor ever has been, appurtenant to land, but may be transferred from location to location with the permission of the company. In each instance, there are normally two shares to the acre. Canyon Line stock costs $50 per share, is non-assessable, and, theoretically, only Colorado River water is delivered at the rate of $1.05 per miner's inch day. These shares are all located on lands southeast of the City of Corona. The common stock presently costs $185 per share, although the Articles of Incorporation fixed the price at $100 per share, and each share entitles the holder thereof to water allocated by the company but not less than three miner's inch days per month. These shares are assessable. In 1961, each share of common stock was assessed $30. In December, 1961, there were 13,057 shares of stock issued, of which 11,851 were common and 1,206 were Canyon Line shares.

Rate Base

Although the Commission, in its Decision No. 59443, instructed Temescal to develop the original cost of the water system and depreciation reserve requirement in

order that the Commission could establish fair and reasonable rates, Temescal failed to present such material to the Commission for the reason, as stated by its legal counsel, that Temescal and the Commission's staff are not in a position to make recommendations and to make a full showing as to the final rates, service area, and rules. Its counsel further stated that this hearing was for the purpose of determining rates, rules, and a service area on an interim basis. This position was not acquiesced in by the staff lawyer. There is nothing in the record before this Commission at this time to enable it to establish a rate base.

Service Area Controversy

Both the staff and Temescal agree to the outward limits of the total service area (pages 35 and 36 of Exhibit 15, Temescal, and Exhibits 18 and 19, staff). There are islands of land in the service area proposed by the staff on which no stock is presently applicable. Temescal proposes that its service area include only land on which stock is applicable, and suggests that as the stock is transferred to another area the area be redefined. The staff suggests that the area should include land excluded by Temescal.

The record herein shows that Temescal has from time to time transferred shares of stock to another area. Inasmuch as we are attempting to define a service area, it is impractical, if not impossible, to permit Temescal to shift its services. For this reason, we concur in the staff's request that the outward limits of the service area be defined and that Temescal be required to serve all land within such outward boundaries. We find that Temescal has dedicated its plant and water

to serve the service area depicted on Exhibits 18 and 19 herein.

It should be further noted, however, that there are some domestic services in the City of Corona and in the area south and east thereof served by Corona which were held by the Commission to be services of Temescal. In addition, there are some Corona services served from Temescal's lines. Temescal has no domestic tariffs and is desirous of terminating any domestic service. Accordingly, these parties have filed Application No. 44648 whereby authority is requested for each to temporarily furnish some services to the other's customers, and Application No. 44939 whereby Temescal will sell to Corona a portion of its No. 3 transmission line, thus removing Temescal's domestic services. The Commission granted these applications by Decision No. 65087 and Decision No. 65088, respectively. No rates for domestic service will be established herein.

Rates

Temescal proposes two rates for general water service and limited water service. These rates are as follows:

GENERAL WATER SERVICE

RATES

Minimum Charge	*Per Annum*
	$26.00 per share of stock
Water Charge	
First 36.5 miner's inch days* per share	0.71 per M.I.D.*
Over 36.5 miner's inch days* per share	1.00 per M.I.D.*

*1/50 cubic feet per second per day

SPECIAL CONDITIONS

1. Service will be rendered only to shareholders owning common stock of Temescal Water Company.
2. Service is limited to capacity of system and is on a scheduled basis.
3. Service rendered to Corona City Water Company under this schedule is rendered on demand of Corona City Water Company.
4. Annual minimum charge will be billed November 1 of each year and is delinquent December 1.
5. Charges for water used will be billed monthly.

LIMITED WATER SERVICE

RATES

For all water delivered per miner's inch day $1.10

SPECIAL CONDITIONS

1. Service will be rendered only to shareholders in Temescal Canyon owning Canyon Line stock of Temescal Water Company.
2. Service is limited to availability of water from Western Municipal Water District of Riverside County and is on a scheduled basis.
3. Charges for water used will be billed monthly.

The staff proposes two rates, namely, annual measured resale service, and annual measured irrigation service (Appendix A, pages 1 through 3 of Exhibit 17).

ANNUAL MEASURED RESALE SERVICE

RATES	Per Miner's Inch Day Per Year
Annual Quantity Rate:	
For all water delivered	$ 0.80
Annual Minimum Charge	64.000.00

The Annual Minimum Charge will entitle the customer to the quantity of water each year which the annual minimum charge will purchase at the Annual Quantity Rate.

SPECIAL CONDITIONS

1. The annual minimum charge applies to service during the 12-month period beginning January 1. and is due in advance. The customer may elect to pay the annual minimum charge in advance on a monthly basis equal to one twelfth of the annual minimum charge.
2. Charges for water used in excess of the annual allowance under the annual minimum charge shall be billed monthly.
3. A miner's inch day is defined as the volume resulting from a continuous flow of one fiftieth of a cubic foot of water per second over a 24-hour period.

ANNUAL MEASURED IRRIGATION SERVICE

RATES.	Per Miner's Inch Day Per Year
Annual Quantity Rate:	
For all water delivered	$ 0.70
Annual Minimum Charge:	
For each acre	42.00

The Annual Minimum Charge will entitle the customer to the quantity of water each year which the annual minimum charge will purchase at the Annual Quantity Rate.

SPECIAL CONDITIONS

1. Written application for service under this schedule shall be made on or before the first day of the calendar year in which service is desired. Such application shall indicate the number of acres to be irrigated.
2. Water shall be delivered at pressures available.
3. The water supplied under this schedule is untreated water from open ditches, canals, conduits and flumes. The Company does not represent or guarantee that any water delivered hereunder is potable or of a quality suitable for human consumption. Any customer who uses said water or makes it available or offers it to others for human consumption shall take all necessary precautions to make the same potable and shall assume all risks and liabilities in connection therewith.
4. The annual minimum charge applies to service during the 12-month period commencing January 1, and is due in advance. The customer may elect to pay the annual minimum charge in advance on a bimonthly basis equal to one sixth of the annual minimum charge.
5. Charges for water used in excess of the annual allowance under the annual minimum charge shall be billed bimonthly.

6. A miner's inch day is defined as the volume resulting from a continuous flow of one fiftieth of a cubic foot of water per second over a 24-hour period.

Temescal's general service rate is for water consumers owning common stock in the company. Such service would include service to Corona City Water Company. The limited service rate would be available only to holders of Canyon Line stock. The evidence in support of Temescal's request is that the rates proposed are in conformity with the existing Articles of Incorporation and the by-laws of the corporation, will not impair any existing rights of stockholders, and are sufficient until such time as the water company is able to complete its rate study and secure whatever rates the Commission determines proper based upon its rate base. It should be noted that Temescal's proposal would conform to its existing practices. From the outset of its operations, Temescal's method of securing revenues as to its common stock only has been and now is to issue stock to the landowner, normally two shares per acre of land supplied with water, the directors determine the amount of water to be supplied pursuant to each share of stock, and this amount of water is furnished to the shareholder. At the end of the year, an assessment is levied against each share to provide additional revenue. This assessment has varied between $15 in 1956 and $30 in 1961, and the annual entitlement in miner's inch days has varied between 29.8 in 1957 and 43.6 in 1961. This water is allocated by months and when this water has been used each month, the shareholder is required to pay for any extra water he purchases. This water is, at present, furnished at the rate of $1.10 per miner's

inch day. Each water user must use his water entitlement in the month in which granted, except for a five percent carry-over to the succeeding month. Corona City Water Company is the largest individual stockholder of Temescal and it secures its water the same as other common stockholders, except for a special provision allowing it to accumulate its unused water under its entitlement.

The Canyon Line shares are non-assessable.

Temescal's arguments in favor of its proposed rates are that, in an ordinary utility operation, the plant and facilities necessary to furnish service are obtained through the investment of risk capital in the utility by stockholders; that for their investment, they expect to receive a fair return on the monies invested; that this profit motive explains the fundamental reason for the detailed analyses of rate base and the determination of a reasonable rate of return to arrive at a reasonable rate structure for the utility. In addition, it is argued that the Commission must seek to assure a sound financial operation for the utility, including a fair rate of return on investment to its stockholders and, at the same time, protect the public by assuring the consumer the highest possible service at the lowest feasible rates.

Temescal urges that these principles have no rational application to what it terms a "regulated mutual water company" such as it; that the stockholders acquired their stock not as investors seeking returns on their investments but as water users seeking water rights in order to obtain the water which they desire; that they chose this mutual company to obtain their water at the lowest price, that is, at cost; and that inasmuch as the

stockholders are the consumers, they cannot benefit by increasing the costs to themselves in order that the company may pay them a return on their investments.

It is further argued that it is one of the advantageous characteristics of a nonprofit mutual water company that it is exempt from federal income tax; that public utility regulation of such a mutual does not destroy the exemption, as long as the nonprofit character of the operation prevails; and that if a rate structure reflecting a profit is established, a tax would be payable and the net cost to the consumer-stockholder must necessarily increase.

It is further argued that a condition precedent to the feasibility of a nonprofit rate structure is the fact that the stockholders in a company such as Temescal are not ordinary investors; that if they were merely investors, they would have a right to receive a rate of return on their investment and consequently a right to object to any rate structure which would deny them such a return; that the nonprofit rate is only feasible where, as in the case of a "regulated mutual water company," the water right is owned by the stockholder and water is served to stockholders only; that in these circumstances, the system subject to utility regulation is wholly owned by its consumers and the dominant interest of those consumers is in the delivery of water at the lowest possible cost; and that this situation makes wholly incongruous any suggestion that rates be established to give shareholders a fair return on their investment, to their own detriment.

Temescal's evidence is that it proposes to deliver water at a nonprofit, non-loss rate. The rates it proposes

would be subject to assessment or refund after the costs for a particular year are determined. The principal reasons for such proposal are stated to be that mutual water companies are not subject to federal income tax and actually, under the federal laws, enjoy a benefit not extended to others in that 15 percent of their total incomes may be derived from non-water operations and, in keeping the rate at a nonprofit rate, Temescal would not be subject to tax on any amount over and above the actual cost of operations.

The company witness stated that the proposed general water service rates would permit the stockholders to secure 36½ miner's inch days of water at 71 cents per miner's inch day which, it is alleged, is very close to the historic average annual common stock entitlement. The limited water service rate would be for Canyon Line shareholders and would be $1.16 per miner's inch day, an increase of eleven cents per miner's inch day.

The company proposes that after the end of each calendar year and before May 1 of the following year, a determination shall be made as to whether the revenues from water charges to common stockholders exceed or failed to meet operating costs and expenses. If a surplus exists, a refund or credit shall be made to all commonstockholder water users during the year in question in proportion to the quantity of water delivered. In the event of a deficit, an assessment shall be made. This involves a modification of present policy in that both stock water and extra water participate in any refunds or assessments to adjust the year to a nonprofit basis. Thus, the differential between the charge for stock water and extra water, approximately 30 cents, will re-

main relatively constant, with both types of water participating in the advantages and disadvantages of each year's operations.

It is claimed that Temescal has certain capital assets none of which are devoted wholly to water production, distribution or storage. Some are partially involved in such operating matters, and some are wholly nonoperating properties. There have heretofore been rents and profits derived from the operation of such property but unrelated to storage, production, and distribution of water. It is stated that since the income derived from these sources is attributable to the investment of capital rather than the use of water, any net proceeds from such activities may be retained by the company in reserve for capital purposes or credited proportionately to the accounts of common stockholders based on their stock ownership.

The company's evidence is, further, that the 30-cent differential between stock water and extra water is purportedly based on a six percent return on the present cost of common shares of $185.

In explanation of the increased cost of water to Canyon Line shareholders, the company's witness testified that the cost to such shareholders is directly related to the cost of raw water which the company purchases from the Western Municipal Water District of Riverside County; that, between the time the present rate of $1.05 per miner's inch day was determined and the present time, there have been increases totaling $1.50 per acre-foot in the cost of water to the company and the proposal allegedly applies the fact that the company must purchase 1.84 acre-feet of water to deliver one acre-foot of water, the cost of which to the company

has increased $1.50 since 1956. This total cost of water per acre-foot delivered is calculated (page 51 of Exhibit 15) to equal $2.76 per acre-foot or 11 cents per miner's inch day. (It should be noted, however, that the comparison table on the last page of Exhibit 16 shows that practically all water produced was sold to consumers.)

Temescal has not prepared a depreciation study for this proceeding. It did make, however, a depreciation expense study in 1955 when it appeared that, as a result of a condemnation action relative to Railroad Canyon, it might be required to pay a federal income tax. This study, prepared for such purpose and not for rate-making purposes as shown in Exhibit 16, showed depreciation expense of $30,461.08 in 1961. This, it is alleged, is the best figure available at present and is the figure the company is willing to start with. There has been no cost of service study made.

If the company operates on a nonprofit basis, it would secure capital from stock sales, long-term borrowing, capital reserve, from non-utility income, from depreciation expense, or from capital assessments.

The staff's position is that in order to develop proper utility rates, a results of operation report, and a cost of service study should be made; that this is not possible at this time as Temescal has not completed either its original cost study or depreciation reserve requirement applicable to its water system properties. Accordingly, proposed rates, heretofore set forth, were developed, designed to bring in revenues and result in charges approximating those now received from Temescal's irrigation and resale service.

According to the staff witness, Temescal's common stock assessments and annual entitlements for the years 1956 through 1961 were as follows:

ASSESSMENT AND ENTITLEMENT OF WATER PER SHARE OF STOCK

Description						
Year	1956	1957	1958	1959	1960	1961
Assessment	$ 15	$ 18	$ 21	$ 21	$ 25	$ 30
Annual entitlement in miner's inch days	41.3	29.8	39.4	42.7	35.7	43.6
Average entitlement in miner's inch days from 1956 to 1961						38.7

The increased assessment was stated by the witness to have been caused partly by inflation and partly by increased costs for purchased water. He said the 1961 water purchases were extremely high, being 43 percent of the water sold, and are reflected in the 1961 assessment rate. Consequently, he considered the 1960 assessment of $25 more reasonable and adopted it. In that year the company purchased 30 percent of its water, which figure is above average, including 1961. He also stated that the facts do not bear out Temescal's contention that Canyon Line water deliveries are on a surplus basis in that, in spite of unusually low rainfall which required the purchase by Temescal of Metropolitan Water District water to make up its deficiencies, deliveries to Canyon Line shareholders have been increasing continuously since the service was instituted and a differential in charges would appear discriminatory. The rates the staff proposed are designed to recover the sum of revenues levied from (1) assessments of $25 per regular share of stock, (2) the average revenues derived from excess water charges over the past six years, and (3) Canyon Line share revenues

for the year 1961. The average rate is 70 cents per miner's inch day. The proposed minimum charge per acre is based on the minimum entitlement per acre over the past six years.

In determining rates for Corona City Water Company, the witness related the water to the number of shares it owned and not to the number of acres of land. Water used in excess of its entitlement has been paid for at the rate of $1.10 per miner's inch day. Its average entitlement over the past six years was 81,350 miner's inch days, but its average annual usage per customer applied to the present number of customers approximated 123,860 miner's inch days. The rates proposed are designed to recover the revenues derived from the sum of assessments per share of $25 and the revenues derived from excess water charges at $1.10 per miner's inch day for usage in excess of the entitlement.

The proposed rates would, it is claimed, bring in revenues from water sales comparable to the revenues presently derived from water assessments, extra water charges and Canyon Line sales. Because the utility's books do not properly segregate expenses from capital expenditures, it could not be determined whether or not these rates will require the addition of non-utility income to pay the total expenses of the company.

A staff financial examiner testified that he examined the books and records of the company in the course of an assignment which involved a determination as to whether the utility had made an original cost study of its utility properties, had determined depreciation reserve requirements on such properties, and had prepared a cost of service study. He stated that in the

examination of these records he was able to determine that not only did the books not reflect the original cost of the properties but that the books were based upon several appraisals at various dates. He also determined that the most recent recording with respect to depreciation reserve was in 1956 and that this depreciation reserve was based upon certain studies prepared entirely on a basis other than a determination based upon original cost. It was for income tax purpose alone and he was unable to ascertain whether or not such depreciation was in fact depreciation based upon original cost.

In addition to a determination with respect to investment in utility plant and the recorded depreciation reserve, the witness also made an extensive analysis of operating accounts of the company, including operating expense, payroll, and other items of expense. It was his finding in this regard that over the years the utility had maintained its books on a basis not in accordance with the Uniform System of Accounts but not differing materially from the manner in which books are normally kept in mutual water companies.

In this respect it was determined that there was no adequate differentiation between expenditures of a capital nature and items of an expense nature and for this reason any reliance upon operating expense recorded on the books of the company, or reflected in any operating statement prepared by the CPA engaged by the company, would not be appropriate in that there are several areas of expenditures which have been recorded as expense and which, in the staff's estimation, should have been recorded as addition to utility plant accounts.

Temescal produced evidence purporting to show that under the staff-proposed rates the total revenues from

water sales would be $40.547 short of total expenses. A witness for respondent stated that this computation does not include revenues from non-utility leases and property rentals but does include all expenses, including non-utility expenses.

The staff stated that it is unable and unwilling to adopt and utilize recorded operating expenses as a measure of the revenue requirements because of lack of showing that such recorded expenses are wholly attributable to water operations. The staff recommended specific rate schedules to be filed by Temescal, but indicated it would have no objection to alternative proposals which might be presented by the utility to achieve its stated objective of collecting revenues equal to reasonable water operating expenses alone. There is in the record, however, nothing on which the Commission could determine the water operating expenses alone.

Temescal's proposal is that a rate designed to recover the expenses of operation be established and that the consumers be informed through the rate schedule that at the end of each year an assessment or refund would be made proportionately to all water delivered in order to adjust to a nonprofit operation. Accounting, in arriving at such nonprofit operations, would be based upon an analysis of the books of the company which will be maintained in accordance with the Uniform System of Accounts.

In support of its request for authority to fix rates based on annual revenues, Temescal's witness cited Case No. 4716, Decision No. 38786, dated March 26, 1946, concerning Southern Counties Gas Company of California. While this order did permit adjustments, it was based on evidence which indicated the rate base

plus additions and less retirements. In addition, it was a post-World War II emergency action and cannot be used as a criterion here.

We will not accept the company's proposal for non-fixed rates. The staff's proposed rates and rules we hereby find to be reasonable and they will be adopted and placed in effect until Temescal is prepared to present evidence upon which a different set of rates and rules could be based. If the rates and charges herein authorized should result in a rate increase as to any customer, we find that the rates and charges herein authorized are reasonable and that the present rates and charges, insofar as they differ from those prescribed herein, are for the future unjust and unreasonable.

The Stockholders

It is urged by a representative of a group of shareholders that comprehensive regulation of Temescal, because of its public service functions, may not be used as a device to impinge upon the shareowners' rights and that they considered their shares constitute ownership of a right in the water sources of Temescal.

This Commission found, however (Decision No. 59443, supra), that Temescal is a public utility water corporation which has dedicated its properties to public use. Such properties include all of Temescal's sources of supply. Such finding was affirmed by the California Supreme Court (*Corona City Water Co. v. Public Utilities Commission*, 54 Cal. 2d 834, decided November 25, 1960). It thus appears that the question of dedication is no longer open to argument.

We see no reason to make an interim order in this case.

ORDER

IT IS ORDERED that:

1. Temescal Water Company shall file with this Commission within sixty days after the effective date hereof and in conformity with General Order No. 96-A, its schedules of rates attached to this order as Appendix A and, upon not less than five days' notice to the Commission and to the public, to make such rates effective for service rendered on and after July 1, 1963.

2. Before December 31, 1963, Temescal Water Company shall complete its studies of the original cost of its water system properties used and useful in the public service, together with the depreciation reserve requirement applicable thereto, as well as a cost of service study, and on or before said date shall file four copies of such studies with this Commission.

3. Within forty-five days after the effective date of this order, Temescal Water Company shall file with this Commission, in conformity with General Order No. 96-A, and in a manner acceptable to the Commission, rules governing service to customers essentially as presented in Exhibit 20 in this proceeding, tariff service area maps which incorporate all of the service area designated on Exhibits 18 and 19, and copies of printed forms normally used in connection with customer services. Such rules, tariff service area map, and forms shall become effective upon five days' notice to the Commission and to the public after filing as hereinabove provided.

4. Within sixty days after the effective date of this order, Temescal Water Company shall file with the Commission four copies of a comprehensive map drawn

to an indicated scale of not more than 600 feet to the inch, delineating by appropriate markings the various tracts of land and territory served; the principal water production, storage, and distribution facilities; and the locations of its various water system properties. Concurrently with the filing of such map or maps, Temescal Water Company shall file four copies of a statement showing all stock pursuant to which it serves water, the number of shares of such stock, the water entitlement of each share of stock, and the name and address of the company issuing such stock.

5. Applicant shall file with the Commission a report, or reports, as required by General Order No. 24-A, which order, insofar as applicable, is made a part of this order.

The effective date of this order shall be twenty days after the date hereof.

Dated at San Francisco, California, this 19th day of March, 1963.

Peter E. Mitchell
Everett C. McKeage
Frederick B. Holoboff
William M. Bennett
Commissioners

Commissioner George G. Grover did not participate in the disposition of this proceeding.

APPENDIX A

Page 1 of 3

Schedule No. 6MA

ANNUAL MEASURED RESALE SERVICE

APPLICABILITY

Applicable to all measured water service furnished for resale purposes on an annual basis.

TERRITORY

Corona and vicinity, Riverside County.

RATES

	Per Miner's Inch Day Per Year
Annual Quantity Rate:	
For all water delivered	$ 0.80
Annual Minimum Charge	64,000.00

The Annual Minimum Charge will entitle the customer to the quantity of water each year, which the annual minimum charge will purchase at the Annual Quantity Rate.

SPECIAL CONDITIONS

1. The annual minimum charge applies to service during the 12-month period beginning January 1, and is due in advance. The customer may elect to pay the annual minimum charge in advance on a monthly basis equal to one twelfth of the annual minimum charge.

2. Charges for water used in excess of the annual allowance under the annual minimum charge shall be billed monthly.

3. A miner's inch day is defined as the volume resulting from a continuous flow of one fiftieth of a cubic foot of water per second over a 24-hour period.

APPENDIX A

Pages 2 of 3

Schedule No. 3MA

ANNUAL MEASURED IRRIGATION SERVICE

APPLICABILITY

Applicable to all measured irrigation service furnished on an annual basis.

TERRITORY

Corona and vicinity and in Temescal Canyon, extending southeasterly from Corona, Riverside County.

RATES

	Per Miner's Inch Day Per Year
Annual Quantity Rate:	
For all water delivered	$ 0.70
Annual Minimum Charge:	
For each acre	42.00

The Annual Minimum Charge will entitle the customer to the quantity of water each year, which the annual minimum charge will purchase at the Annual Quantity Rate.

SPECIAL CONDITIONS

1. Written application for service under this schedule shall be made on or before the first day of the calendar year in which service is desired. Such application shall indicate the number of acres to be irrigated.

2. Water shall be delivered at pressures available.

3. The water supplied under this schedule is untreated water from open ditches, canals, conduits and flume. The Company does not represent or guarantee that any water delivered hereunder is potable or of a

quality suitable for human consumption. Any customer who uses said water or makes it available or offers it to others for human consumption shall take all necessary precautions to make the same potable and shall assume all risks and liabilities in connection therewith.

APPENDIX A

Page 3 of 3

Schedule No. 3MA

ANNUAL MEASURED IRRIGATION SERVICE

SPECIAL CONDITIONS (Continued)

4. The annual minimum charge applies to service during the 12-month period commencing January 1, and is due in advance. The customer may elect to pay the annual minimum charge in advance on a bimonthly basis equal to one sixth of the annual minimum charge.

5. Charges for water used in excess of the annual allowance under the annual minimum charge shall be billed bimonthly.

6. A miner's inch day is defined as the volume resulting from a continuous flow of one fiftieth of a cubic foot of water per second over a 24 hour period.

APPENDIX B.

Pertinent Text of Constitutional Provisions and Statutes Involved.

"No estate shall . . . . pass any . . . . law impairing the obligation of contracts."

Art. I, Sec. 10, Const. of U.S.

". . . nor shall any state deprive any person of . . . property, without due process of law."

Amdt XIV, Sec. 1, Const. of U.S.

"Every private corporation, and every individual or association of individuals, owning, operation, managing, or controlling any commercial railroad, interurban railroad, street railroad, canal, pipe line, plant, or equipment, or any part of such railroad, canal, pipe line, plant or equipment within this State, for the transportation or conveyance of passengers, or express matter, or freight of any kind, including crude oil, or for the transmission of telephone or telegraph messages, or for the production, generation, transmission, delivery or furnishing of heat, light, water or power or for the furnishing of storage or wharfage facilities, either directly or indirectly, to or for the public, and every common carrier, is hereby declared to be a public utility subject to such control and regulation by the Railroad Commission as may be provided by the Legislature, and every class of private corporations, individuals, or associations of individuals hereafter declared by the Legislature to be public utilities shall likewise be subject to such control and regulation. The Railroad Commission shall have and exercise such power and jurisdiction to supervise and regulate public utilities, in the State of California, and to fix the rates to be charged for commodities fur-

nished, or services rendered by public utilities as shall be conferred upon it by the Legislature, and the right of the Legislature to confer powers upon the Railroad Commission respecting public utilities is hereby declared to be plenary and to be unlimited by any provision of this Constitution . . ."

Art. 12, Sec. 23, Const. of Calif. (The Railroad Commission has since been designated the "Public Utilities Commission". Art. 12, Sec. 22, Const. of Calif.)

"After any order or decision has been made by the commission, any party to the action or proceeding, or any stockholder or bondholder or other party pecuniarily interested in the public utility affected, may apply for a rehearing. The commission may grant and hold a rehearing on those matters, if in its judgment sufficient reason is made to appear. No cause of action arising out of any order or decision of the commission shall accrue in any court to any corporation or person unless the corporation or person has made, before the effective date of the order or decision, application to the commission for a rehearing."

Sec. 1731, Calif. P.U. Code.

"The application for a rehearing shall set forth specifically the ground or grounds on which the applicant considers the decision or order to be unlawful. No corporation or person shall in any court urge or rely on any ground not so set forth in the application."

Sec. 1732, Calif. P.U. Code.

"Within 30 days after the application for a rehearing is denied . . . the applicant may apply to the Supreme Court of this State for a writ of certiorari or

review for the purpose of having the lawfulness of the original order or decision or of the order or decision on rehearing inquired into and determined . . ."

Sec. 1756, Calif. P.U. Code.

"No court of this State, except the Supreme Court to the extent specified in this article, shall have jurisdiction to review, reverse, correct, or annul any order or decision of the commission or to suspend or delay the execution or operation thereof, or to enjoin, restrain, or interfere with the commission in the performance of its official duties, except that the writ of mandamus shall lie from the Supreme Court to the commission in all proper cases."

Sec. 1759, Calif. P.U. Code.

APPENDIX C.

Quotations of Specific Portions of the Record to Show the Federal Question Was Timely and Properly Raised.

Temescal Water Company

Petition for rehearing of Decision No. 65115 before Public Utilities Commission of the State of California [Tem. R. 51-52].

> "The rates . . . recommended [by the commission's staff expert] and which are now established by the Commission are both arbitrary and thereby violative of the due process clauses of the California and United States Constitutions."

Temescal Water Company

Petition for writ of review before the Supreme Court of the State of California [Tem. R. 11-12].

> "*Grounds for Review.* Decision No. 65115 is unlawful in that:
>
> (a) Said Decision is in violation of Article I, Section 10 and Amendment XIV of the Constitution of the United States and Article I, Section 13 of the Constitution of California, in that:
>
> (1) It denies Temescal substantive due process by ordering the establishment of rates at a confiscatory level reflecting no return on investment and forcing the utility to operate at a loss.
>
> (2) It denies Temescal substantive due process and impairs the obligation of its contracts to its irrigation shareholders by finding that the water rights of said shareholders are dedicated to public use in the utility sense, and orders the

service of water to lands to which no water service has heretofore been made.

(3) It denies Temescal procedural due process of law in that said utility was forced to hearing, and a decision and order setting rates was entered, before either Temescal or the Commission staff could complete studies establishing rate base or utility expenses."

James A. Stein

Petition for rehearing of Decision No. 65115 before Public Utilities Commission of the State of California [St. R. 46-47].

"Decision No. 65115 is contrary to the Constitution of the State of California and of the United States, and is beyond the jurisdiction of the Public Utilities Commission. By it, the irrigation shareowners will be deprived of property without due process of law, and their private property be taken without just compensation having been made therefor, and the obligation of their private contract with the Temescal Water Company be impaired."

James A. Stein

Application for a writ of certiorari before the Supreme Court of the State of California [St. R. 7-9].

"6. Upon Decision No. 65115 being made, the shareowners of the Temescal Water Company appearing as interested parties submitted a petition for rehearing . . . raising the following objections:

(1) The Decision Would Abrogate the Private Contracts By Which Rates Are Established For

Irrigation Water Delivered By Temescal to its Shareowners. These Private Rights of the Shareowners Are Not Subject to Public Regulation.

(2) The Decision Would Abrogate the Provisions of the Articles and By-Laws of Temescal Which Obligate Temescal, as a Matter of Private Contract Not Subject to Public Regulation, to Deliver Irrigation Water on the Terms and Conditions Specified in the Articles and By-Laws.

(3) The Decision Would Subject to Public Regulation the Private Vested Water Rights of the Irrigation Shareowner of Temescal, Which Rights Have Never Been Dedicated to Public Use.

(4) The Decision Would Compel Temescal to Extend Its Water Service. The Record Shows There is No Sufficient Supply of Water For Such Extension.

(5) The Decision Would Prevent Temescal From Resuming Its Status As a Strictly Mutual Company By Terminating Its Public Utility Activities.

8. The petition for rehearing was nevertheless denied. . . .

9. Decision No. 65115 and the order denying a rehearing thereupon is unlawful for the reasons specified in the petition for rehearing made by the shareowners of Temescal Water Company appearing as interested parties. By it, the irrigation shareowners of Temescal will be deprived of prop-

erty without due process of law, and their private property be taken without just compensation having been made therefor, and the obligation of their private contract with the Temescal Water Company be impaired."

SUPREME COURT, U. S.

Office-Supreme Court, U.S.
FILED
JAN 10 1964
JOHN F. DAVIS, CLERK

In the Supreme Court of the United States

OCTOBER TERM, 1963

No. 624

TEMESCAL WATER COMPANY; and JAMES A. STEIN, on his own behalf and on the behalf of shareholders of Temescal Water Company,

Petitioners,

vs,

THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA,

Respondent.

On Petition for Writ of Certiorari to the Supreme Court of the State of California

Brief for Public Utilities Commission of the State of California in Opposition

RICHARD E. TUTTLE
J. THOMASON PHELPS
MARY MORAN PAJALICH
HECTOR ANNINOS
5072 State Building
San Francisco 2, California

Attorneys for Respondent Public Utilities Commission of the State of California and the People of the State of California

SORG PRINTING COMPANY OF CALIFORNIA, 180 FIRST STREET, SAN FRANCISCO 5

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Brief for Public Utilities Commission of the State of California in Opposition

OPINIONS BELOW

Petitioners ask review of Decision No. 65115 (60 Cal. P.U.C. 669 (1963)), dated March 19, 1963, of the Public Utilities Commission of the State of California, as affirmed without opinion by the Supreme Court of the State of California on August 20, 1963.

Decision No. 59443 (57 Cal. P.U.C. 474 (1959)) of the Public Utilities Commission of the State of California and

the opinion of the Supreme Court of California in *Corona City Water Company v. Public Utilities Commission*, 54 Cal. 2d 834; 357 P.2d 301 (1960), are improperly included under the heading "Citation of Opinions Below", page 1 of petition. Said decision and opinion are not the subject of the review sought here, having long been final and *res judicata* as to the issues raised therein.

JURISDICTION

The jurisdictional requisites are adequately set forth in the petition.

STATUTES INVOLVED

Cited at page 3 of the petition, and set forth in Appendix B thereof, is Article XII, Section 23 of the Constitution of the State of California. That section undertakes generally to define what constitutes a public utility. It is submitted that in this respect the section has no relevance in this proceeding since the issue of whether or not petitioner Temescal Water Company is a public utility was determined in the affirmative by Decision No. 59443 (57 Cal. P.U.C. 474 (1959)) of the Public Utilities Commission of the State of California, and by the Supreme Court of California in *Corona City Water Company v. Public Utilities Commission*, 54 Cal. 2d 834; 357 P.2d 301 (1960), such decision and opinion having become final.

ARGUMENT

I. The Decision Is in Accord With the Evidence and Is Reasonable in the Circumstances.

1. Temescal's Proposed Non-Profit Rate Structure.

Decision No. 59443 (Appendix A to petition for writ), issued by respondent Commission on December 29, 1959, found Temescal Water Company to be a public utility sub-

ject to the jurisdiction, supervision and control of the Commission. That finding of public utility status was affirmed by the Supreme Court of California in *Corona City Water Co. v. Public Utilities Commission*, 54 Cal. 2d 834; 357 P.2d 301 (p. 13 of petition for writ), on November 25, 1960, (rehearing denied December 21, 1960). No further appeal was taken and Decision No. 59443 and the opinion of the California Supreme Court have, of course, long since become final. The effect of the foregoing was to subject petitioner to the jurisdiction of this Commission as set forth and defined in the Constitution of the State of California and the Public Utilities Code of California. This jurisdiction extends generally to rates and charges of public utilities. (Article XII, Sect. 23, Constitution of the State of California Sections 451-495, Public Utilities Code of California).

Pursuant to the Commission's rate jurisdiction, Decision No. 59443 reopened the proceeding for the purpose of determining the original cost of the water system properties used in public service, together with the depreciation reserve requirement applicable thereto, and the establishment thereafter of just and reasonable rates (petition for writ, p. 17). Original cost and depreciation studies and determinations are, of course, necessary before rates can be fixed upon the usual rate base and rate of return method.

It is clear from reference to letters attached as Exhibits E, F and G to Temescal's petition for writ of review to the California Supreme Court (Tem. R. pp. 62-67),[1] that on February 8, 1962, well more than one year after Decision No. 59443 was affirmed, Temescal was still attempting to complete the necessary plant and depreciation studies with

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1. References to the record will be as indicated in the footnote at page 4 of the petition for writ.

the assistance of a person possessed of no experience in public utility rate proceedings. By March 6, 1962, it had become apparent to Temescal that they would have to start again with their studies with the assistance of a qualified engineering advisory firm (See Tem. R. pp. 65-66), but that the additional time required would necessitate taking the proceeding off calendar for an indefinite period. At page 66 (Tem. R.) Temescal expressed its willingness to proceed with a limited presentation, if the Commission was agreeable, upon a May 1962 date which Temescal had proposed in a prior letter (Tem. R. p. 64). In a reply letter (Tem. R. p. 67) the Commission agreed to a procedure contemplating a limited showing to result in interim or temporary rates, to be followed by further hearings at a later date when Temescal's comprehensive studies were completed, after which a different and final order might issue. That Temescal fully understood and consented to this method of proceeding is also evident from a portion of its counsel's opening statement which is quoted in this Commission's answer to the petition for review directed to the California Supreme Court (Tem. R. p. 102; see also Tem. R. pp. 18-19).

At the hearings Temescal made its novel proposal for "non-profit rates". Temescal claimed that as a nonprofit mutual water company it had been exempt from the federal income tax, as well as receiving certain other tax benefits for non-water operations. Since Temescal's stockholders and consumers were one and the same, no advantage could be gained by earning a return on investment for stockholders when the money would have to come from increased rates to the stockholders themselves in their identity as consumers. In fact, susceptibility for the first time to income taxes would leave them in a worse position. Temescal

was of the opinion that nonprofit rates would permit them to continue to enjoy their tax benefits despite their new status as a public utility. To insure nonprofit operation Temescal proposed a year-end determination of whether water revenues exceeded or failed to cover expenses, followed by either a refund or assessment of stockholder-consumers, depending upon the results, in order to achieve the nonprofit objective. Temescal's proposal is set forth in greater detail in Decision No. 65115 complained of here (Tem. R. pp. 25-29), and in this Commission's answer to the petition to the California Supreme Court, in which answer portions of Temescal's principal testimony and exhibit are quoted. (Tem. R. pp. 84-86.)

2. The Rate Proposal of the Commission Staff.

Ultimately approved and adopted by the Commission in Decision No. 65115 was the rate proposal of the Commission staff. The basis of that proposal is set forth in considerable detail in Decision No. 65115. (Tem. R. pp. 31-37.) The staff concluded first that the fixing of proper utility rates would necessarily have to await the completion by Temescal of the original cost and depreciation reserve requirement studies. It therefore proposed rates designed to bring in revenues and result in charges approximating those then being received from Temescal's irrigation and resale services (Tem. R. p. 31).

The staff proposal attempted to accommodate Temescal's stated objective of nonprofit rates. However, the staff proposal contemplated *fixed* rates since it could not accept the suggested device of a year-end assessment-refund provision by which Temescal sought to guarantee nonprofit operation. That provision constitutes, in effect, not only retroactive ratemaking, but retroactive ratemaking by the utility

itself and not with prior approval of the Commission charged by the statutes with the responsibility of fixing rates. Retroactive ratemaking is generally considered to be invalid unless authorized by statutes. (1 Davis, Admin. Law Treatise, § 5.08 (1958) pp. 340-1); *Public Util. Com. v. United Fuel Gas Co.*, 317 U.S. 456, 460-463, (1943); *Transcontinental & W. Air v. Civil Aero. Board*, 336 U.S. 601, (1949)). No such authority can be found in the California Public Utilities Code. Section 454 thereof does state in part as follows in so far as rate *increases* are concerned:

> "No public utility shall raise any rate, or so alter any classification, contract, practice, or rule as to result in any increase in any rate except upon a showing before the commission and a finding by the commission that such increase is justified."

This Commission has held unequivocally (*Re Pacific Tel. & Tel. Co.*, Decision No. 43145, 48 CPUC 823, 836 (1949)) that rates may not be fixed retroactively by the Commission itself, to say nothing of unilateral action of this nature by the public utility. It is the view of this Commission that the assessment-refund provision which Temescal proposed is contrary to the Public Utilities Code and its inherent concept of a fixed and determined rate for the future. This respondent was not disposed to discard or qualify that view in order to accommodate one company's plan to unilaterally vary its rates retroactively so that it might escape payment of federal income taxes.

3. The Evidence.

At page 3 of the petition for writ, under the heading "Questions Presented" appears the allegation that Decision No. 65115 "is not based on evidence or is contrary to evidence." If the first portion of this charge is intended to

mean there was *no* evidence to support the decision, we would first note that this claim was not made in the petitions to the California Supreme Court filed by petitioners herein (See grounds for review set forth in Tem. R. pp. 11-12 and St. R. pp. 7-8), and may not properly be raised before this court. (*California v. Taylor*, 353 U.S. 553, 557, n. 2 (1957); *Lawn v. United States*, 355 U.S. 339, 362, n. 16 (1958)).

If it is assumed that this issue is properly raised here, it would appear to have reference to the remark at page 4 of the petition for writ that there was nothing in the record to enable the Commission to establish a rate base or to determine water operating expenses alone. As to evidence of rate base, it is clear from paragraph I, 1, above, that this proceeding commenced with the understanding that the studies necessary for the determination of rate base had not been completed by Temescal—in fact, hardly commenced—despite the passage of a year and a half from the California Supreme Court's finding of public utility status, and that such evidence would have to await a further hearing.

As to evidence needed to determine water operating expenses alone, this was Temescal's failure. It is apparent from Decision No. 65115 (Tem. R. pp. 35-37) that Temescal's witness conceded that its figures did not include revenues from nonutility sources, but *did* include all expenses, including nonutility expenses. Temescal failed to produce evidence by which the Commission could determine water operating expenses alone. This was one of the principal causes for the rejection of Temescal's rate proposal and the acceptance of the staff proposed rates. As set forth in this Commission's answer to the petitions to the California Supreme Court (Tem. R. 89-91), Temescal's claim

at page 4 of the instant petition for writ, that the staff rate proposal would produce revenues for 1961 in an amount $40,547 short of expenditures, was necessarily rejected by the Commission because of Temescal's inconsistency in excluding nonutility revenues while including nonutility expenses. Also at page 4 of Temescal's petition to this Court is a reference to a figure of $77,440 applicable to the year 1962. That figure was not a part of the hearing record before the Commission, having been forwarded by Temescal in the form of an affidavit several months after the case was submitted, and was not subjected to cross-examination, test or rebuttal. (Tem. R. p. 91).

Also under the heading "Questions Presented" (page 2 of petition for writ) appears the claim that Decision No. 65115 requires Temescal to operate at a loss. That statement is misleading and inaccurate. Rates are ordinarily established for the future with the objective of producing sufficient revenues as will, in the judgment of the rate-making body, bring to the utility a specific authorized rate of return on its investment devoted to utility use. Since the process is performed prospectively, the facts of utility operation do not offer the prospect of exact attainment of the rate of return objective. Various factors which cannot be foreseen occur and affect operations. For example, water consumption may vary widely due to climatic conditions. Expenses such as wages, local taxes, material and supply costs may change substantially. Unanticipated capital expenditures may alter the rate base. While such changes occur, the authorized rates of necessity remain fixed until the next rate proceeding before the regulatory agency. Since ratemaking is not an exact science, it is apparent that when any rate of return is authorized the best hope can only be that the rate of return actually realized be as close as

possible to the goal. It may be more or it may be less. Perfection cannot be expected when rates are set prospectively.

Considerable judgment and expertise enter into the establishment of utility rates. This Commission utilized its judgment and expertise in selecting from conflicting proposals that *most likely* to achieve the requested goal of nonprofit operation, while yet adhering to recognized principles of prospective ratemaking. The best that could be hoped to be achieved prospectively would be results *substantially close* to Temescal's objective of nonprofit operation. The rates which were authorized here for Temescal are as likely to produce revenues which exceed expenses as they are to produce revenues which do not meet expenses. At the hearing one of Temescal's exhibits contained the following statement in support of the request for a nonprofit rate:

> "Inasmuch as the stockholder is the consumer, he cannot benefit by increasing the costs to himself in order that the company may pay him a return on his investment." (Tem. R. p. 85.)

A relevant inquiry would be whether or not the converse is not also true, i.e., that a stockholder-consumer in this situation is not damaged as a stockholder by a Temescal loss if that loss is traceable to lower water rates paid by him as a consumer.

This respondent submits that there is abundant evidence in the record on the merits and deficiencies of the respective rate-proposals. Decision No. 65115 contains lengthy recitals of such evidence. The Commission performed its duty as an expert regulatory body and authorized those rates which in its judgment were just, reasonable and most likely to achieve the requested nonprofit goal. It should be noted that Decision No. 65115 authorized rates which were intended to be temporary and interim in effect. The following appears in the decision (Tem. R. p. 37):

> "The staff's proposed rates and rules were hereby find to be reasonable and they will be adopted and placed in effect until Temescal is prepared to present evidence upon which a different set of rates and rules could be based."

It would have been preferable here to have had a full and complete showing; thus permitting in the first instance a more accurate determination of just and reasonable rates. However, it was Temescal's own failure to get its accounts in order and to make the necessary studies, despite the passage of a year and a half, which required the rates to be developed as they were. As heretofore noted Temescal agreed to this interim type proceeding. Ordering paragraph 2 of Decision No. 65115 (Tem. R. 38) requires Temescal to complete its studies of original cost, cost of service and depreciation prior to December 31, 1963. Upon such completion Temescal may, if it finds it has justification, come to this Commission for a revision. If Temescal concludes at that time that it prefers to receive a rate of return on its investment rather than accept rates calculated to return its costs alone—even if it has to pay income taxes—this Commission would be pleased to entertain the request.

II. Temescal's Claim That Decision No. 65115 Impairs the Obligation of Contract Is Not Properly Before This Court.

Temescal claims that Decision No. 65115 applies "rates and regulations" for water service which impair existing agreements, thus constituting a taking of property without due process (Petition for Writ, p. 2), and that such "private right in the price and terms" of water are not subject to public regulation (Petition for Writ, pp. 4-5).

Decision No. 65115 does not purport to determine or affect *contract obligations between Temescal* and its share-

holders, or the private rights claimed to be possessed by such shareholders. If such obligations or rights have been affected, they have been affected by this Commission's previous decision, Decision No. 59443 (page 1 of Appendix A to Petition for Writ), later affirmed by the California Supreme Court in 1969 in its *Corona* decision (p. 18 of Appendix A to Petition for Writ). Decision No. 59443 found that Temescal was a public utility water company and ordering paragraph 3 thereof ordered that the case be reopened so that rates and rules might be prescribed pursuant to this Commission's general rate jurisdiction over public utilities. (Article XII, Sec. 23, Constitution of the State of California, see Appendix B to petition for writ; Public Utilities Code of the State of California, Secs. 451-495.) It was the prior decision which subordinated any pre-existing contract rights possessed by Temescal shareholders to the Commission's rate jurisdiction and that decision is, of course, final and the issue of public utility status raised therein *res judicata*.

Even if it were assumed that the issue of the impairment of private contracts or rights has been properly raised in the instant petition for writ, it is obvious that the claim still lacks merit. The California Supreme Court has stated as follows in *Law v. Railroad Commission*, 184 Cal. 737, 739; 195 P. 423, 424 (1921):

> "It has been conclusively settled that the interference with private contracts by the state regulation of rates is but a legitimate effect of a valid exercise of the police power which neither impairs the obligation of a contract nor deprives of property without due process of law." (citing cases)

In *Midland Realty Co. v. Kansas City Power & Light Co.*, 300 U.S. 109, 113, 114 (1937), this Court held that a state

has power to annul and supersede rates previously established by contract between utilities and their customers. (See also *Producers Transportation Co. v. Railroad Commission of the State of California*, 251 U.S. 228, 232 (1920); *Union Dry Goods Co. v. Georgia Public Service Corp.*, 248 U.S. 372, 375 (1919); and *Manigault v. Springs*, 199 U.S. 473, 480 (1905)).

Joining in this petition for writ is James A. Stein, appearing in his own behalf and in behalf of 49 other shareholders, owning in total 4,343 shares of Temescal. This is approximately one-third of the outstanding shares. (Petition for writ, pp. 4-5; see also Tem. R. 95-96). Mr. Stein filed a separate petition for writ before the California Supreme Court (St. R. 1-9) which was denied simultaneously with the denial of Temescal's petition. The claim of impairment of contract obligations and rights is urged principally by Mr. Stein. It was the position of this Commission before the California Supreme Court that Mr. Stein and the shareholders he represents had no standing permitting them to file a separate petition for rehearing. (St. R. pp. 78-79). Since the injury complained of, if established, would affect all shareholders in the same manner and would not injure the 50 shareholders in a manner peculiar to them alone, the type of action contemplated would have been derivative in nature under California law. (*Sutter v. General Petroleum Corp.*, 28 Cal. 2d 525, 530; 170 P.2d 898, 900, 901 (1946); *Gagnon Co., Inc. v. Nevada Desert Inn*, 45 Cal. 2d 448, 453; 289 P.2d 466, 470, 471 (1955); 12 Cal. Jur. 2d. ¶ 213, 214, 215). A shareholder (or shareholders) has no right to bring an action in behalf of a corporation save in exceptional cases where the directors fail to act or are guilty of fraud. (12 Cal. Jur. 2d, ¶ 216.) The prerequisites of a derivative suit were not present before

the California Supreme Court, nor were they even claimed to exist. Lacking any status to appear before the California Supreme Court, Mr. Stein and his fellow shareholders similarly lack status to appear before this Court as parties distinguishable from the Temescal corporate entity. In any event, even if the shareholders had a valid right to separately appear here, the arguments above in answer to Temescal's claim of impairment of contract rights or obligations, would be equally applicable.

At page 6 of the petition for writ, *Allen v. Railroad Commission*, 179 Cal. 68, 175 p. 466 (1918), is cited, apparently in support of Temescal's claim that Decision No. 65115 is in derogation of existing private agreements. The reference does not appear to be relevant, being cited for the proposition that a water company may engage in part in public service and in part in private service and that the latter is not subject to regulation. With this we would not disagree. However, substantially all of Temescal's water was delivered to shareholders and it must be assumed that substantially all of its water production and distribution facilities are utilized for such service. Before the California Supreme Court Temescal did not claim any division of its properties, facilities or services. In *Corona City Water Company v. Public Utilities (supra)*, the court did not touch on the question of dual function or of a dedication in part only. Dedication was found as to the whole, and the opinion is final and the issue *res judicata*. The issue may not now be raised anew and relitigated under the guise of attacking a subsequent rate order of this Commission. Even now petitioners do not state where and how such a division of properties or activities could be made.

CONCLUSION

For the foregoing reasons the petition for writ of certiorari should be denied.

Respectfully submitted,

RICHARD E. TUTTLE
J. THOMASON PHELPS
MARY MORAN PAJALICH
HECTOR ANNINOS
Attorneys for Respondent Public Utilities Commission of the State of California and the People of the State of California

Dated: January 10, 1964.

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IN THE

Supreme Court of the United States

October Term, 1963
No. 624

TEMESCAL WATER COMPANY; and JAMES A. STEIN, on his own behalf and on the behalf of shareholders of Temescal Water Campany,

Petitioners,

vs.

THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA,

Respondent.

On Writ of Certiorari to the Supreme Court of the State of California.

PETITIONERS' REPLY BRIEF.

I.

A Reply to Respondent's First Argument: The Rate Regulation Is Shown to Be Arbitrarily Devised—Not Being Based on Evidence—and to Be Confiscatory.

The first argument made by respondent Public Utilities Commission in its brief is related to the reasonableness of its rate regulation as applied to petitioner Temescal.

Respondent first considers Temescal's "novel p oposa' for 'non-profit rates'" and justifies its rejection of

the proposal on the grounds that the year-end adjustment feature would constitute retroactive ratemaking (Resp. Br. 2-6). Respondent describes the rate adopted in Decision No. 65115 as one "designed to bring in revenues and result in charges approximating" the existing non-profit rates, but eliminating "the suggested device of a year-end assessment refund provision" (Resp. Br. 5).

Pages 6 to 10 of the brief are concerned with the evidence relating to Decision No. 65115. Temescal, in its petition for a rehearing of the decision before the respondent and in its petition for a writ of review to the Supreme Court of the State of California, objected that the decision was arbitrary and was not based on evidence, and that the rate was confiscatory [Tem. R. 9-12, 48-52].

Although respondent submits that there is abundant evidence in the record relating to the rate proposals, it makes no reference to particulars. Respondent claims its ratemaking is based on "Considerable judgment and expertise" (Resp. Br. 9), but the decision itself discloses: 1) "There is nothing in the record before this Commission at this time to enable it to establish a rate base" [Tem. R. 19]; 2) "Because the utility's books do not properly segregate expenses from capital expenditures, it could not be determined whether or not these rates will require the addition of nonutility income to pay the total expenses of the company" [Tem. R. 34]; and 3) "There is in the record, however, nothing on which the Commission could determine the water operating expenses alone" [Tem. R. 36].

Petitioners do not expect ratemaking to be an "exact science" (Resp. Br. 8), but insist that ratemaking based on conjecture is arbitrary, and that when the established rate requires the utility to operate at a loss the federal requirement of due process of law is offended.

II.

A Reply to Respondent's Second Argument: Regulation of Private Water Service Amounts to an Impairment of the Obligation of Contract and the Deprivation of Property Without Due Process of Law.

At the outset of its brief, respondent Public Utilities Commission correctly states that its Decision No. 59443 and the opinion of the Supreme Court of the State of California in *Corona City Water Company v. Public Utilities Commission*, 54 Cal. 2d 843, 357 P. 2d 301, "are not the subject of the review sought here, having been final and *res judicata* as to the issues raised therein" (Resp. Br. 1-2). The question remains: What issues were raised therein?

Petitioners assert that the question of the extent of dedication of property in the Temescal system to public service was not an issue in Decision No. 59443 and in the *Corona* case [Tem. R. 7-8, 47-48, 52, 117-119; Stein R. 4-9, 40-47, 54-56, 94-101]; and petitioners dispute the assumption of respondent that, because the decision and opinion did not specify what property of Temescal was devoted to public service, it follows that all property used or useful in water service is devoted to public service [Tem. R. 93; Stein R. 76].

Respondent concedes that a water company may engage in part in public service and in part in private

service, and that the latter is not subject to public utility regulation (Resp. Br. 13). Although respondent says "Dedication was found as to the whole" (Resp. Br. 13), no reference to the record is given to support the statement, nor does the record support the statement.

> "To hold that property has been dedicated to a public use is not a trivial thing '. . . and such dedication is never presumed without evidence of unequivocal intention' (*Allen v. Railroad Commission*, 179 Cal. 68, 85; 175 Pac. 466, 473)."

There is no evidence in the record that Temescal is engaged in public service as to its irrigation shareowners, which distinguishes this case from the cases cited by respondent under its second argument. To apply rates and regulations to such water service amounts to an impairment of the obligation of contract and the deprivation of property without due process of law.

As to petitioner Stein, that petitioner repeats here what he has urged before: His appearance is not made to advance a shareholder's derivative action but to assert individual, real property rights in the Temescal water system [Stein R. 97-101]. The summary dismissal by the respondent and by the Supreme Court of the State of California [Stein R. 33, 102] of these claims of right judges these claims without ever having given the irrigator-shareowners of Temescal their day in court.

III.

Conclusion.

Petitioners, before coming to this Court, submitted verified petitions for a writ of review to the Supreme Court of the State of California, urging that Decision No. 65115 of the respondent Public Utilities Commission violated their rights under the Constitution of the United States. Their petition was refused by the Supreme Court of the State of California. This petition is their last recourse.

It is no help to petitioners to be told that they can seek an eventual amelioration of respondent's Decision No. 65115 by application for a new rate (Resp. Br. 10), since such application must necessarily be within the boundaries of the excess of jurisdiction complained of here.

Petitioners pray that a writ of certiorari be issued to review the judgment of the Supreme Court of the State of California affirming Decision No. 65115 of the Public Utilities Commission of the State of California.

DONALD D. STARK,
Counsel for Petitioners.